# Promoting Competition in a Consolidating Wireless Industry

August 30, 2011
Presentation to the FCC
United States Cellular Corporation

U.S. Cellular

# Agenda

- Introduction
- Limited Competition from Smaller Carriers
- Competitive Challenges Faced by Smaller Carriers
  - Handset Access
  - Interoperability
  - Roaming
  - Spectrum
  - Special Access
- Divestitures Must Be Open to Smaller Carriers

U.S. Cellular

# Summary

## The Merger Should Not Be Approved Without Significant Conditions and Divestitures

- AT&T attempts to portray USCC — and other small carriers such as MetroPCS, Leap, and Cellular South — as imposing a significant competitive check on the merged company
- This is not true - USCC and other small carriers cannot, even today, impose effective competitive discipline on AT&T and Verizon
- There are significant constraints on the ability of smaller carriers like USCC to compete with the Big 4 today. These include:
  - Lack of access to handsets
  - Lack of competition to provide roaming services
  - Spectrum constraints
  - Lack of competition to provide special access
- Divestitures alone, whether of operations or of spectrum, are not sufficient. A package of conduct remedies is needed to allow smaller carriers to compete

U.S. Cellular

# About USCC

- Founded in 1983 and headquartered in Chicago
- Approx. 6 million customers and over 46 million covered POPs
- Network based on 3G CDMA technology; deploying LTE
- Consistently highest customer satisfaction in region
  - **2011 Customer Service Champion**
    *J.D. Power and Associates*
  - **Highest in Wireless Call Quality Performance**
    *J.D. Power and Associates*
  - **Readers' Choice: Best Wireless Carrier with a Contract Option**
    *PC Magazine*
  - **US Cellular "stands out for value, voice service, and customer service" and was ranked the top provider for post-paid service**
    *Consumer Reports* , January 2011
- Wireless plans offer innovative customer services (free incoming calls, free battery swap, faster phone upgrades, one-and-done contracts, etc.) and value pricing

U.S. Cellular

# Smaller Carriers Face Competitive Barriers

- Smaller carriers face barriers in trying to compete against the Big 4 due to handset exclusivity, lack of interoperability, non-competitive roaming terms, lack of access to spectrum
- USCC targets specific customer segments
  - Award-winning Customer Service and Network Quality
  - Focus on locally-based customers with nationwide coverage
    - Multi-taskers
    - Family plans
    - Business customers
- MetroPCS, Leap, and other smaller carriers focus on prepaid services
  - However, prepaid growth is declining and AT&T and Verizon also offer prepaid choices, as well as a wider range of handsets and plans and broader distribution
    - High churn rate, high expenses, and highly leveraged
    - "[A]s their performance flags, antitrust regulators need to think seriously about how the two minnows will cope in a more concentrated market."
      ---*Wall Street Journal,* August 5, 2011

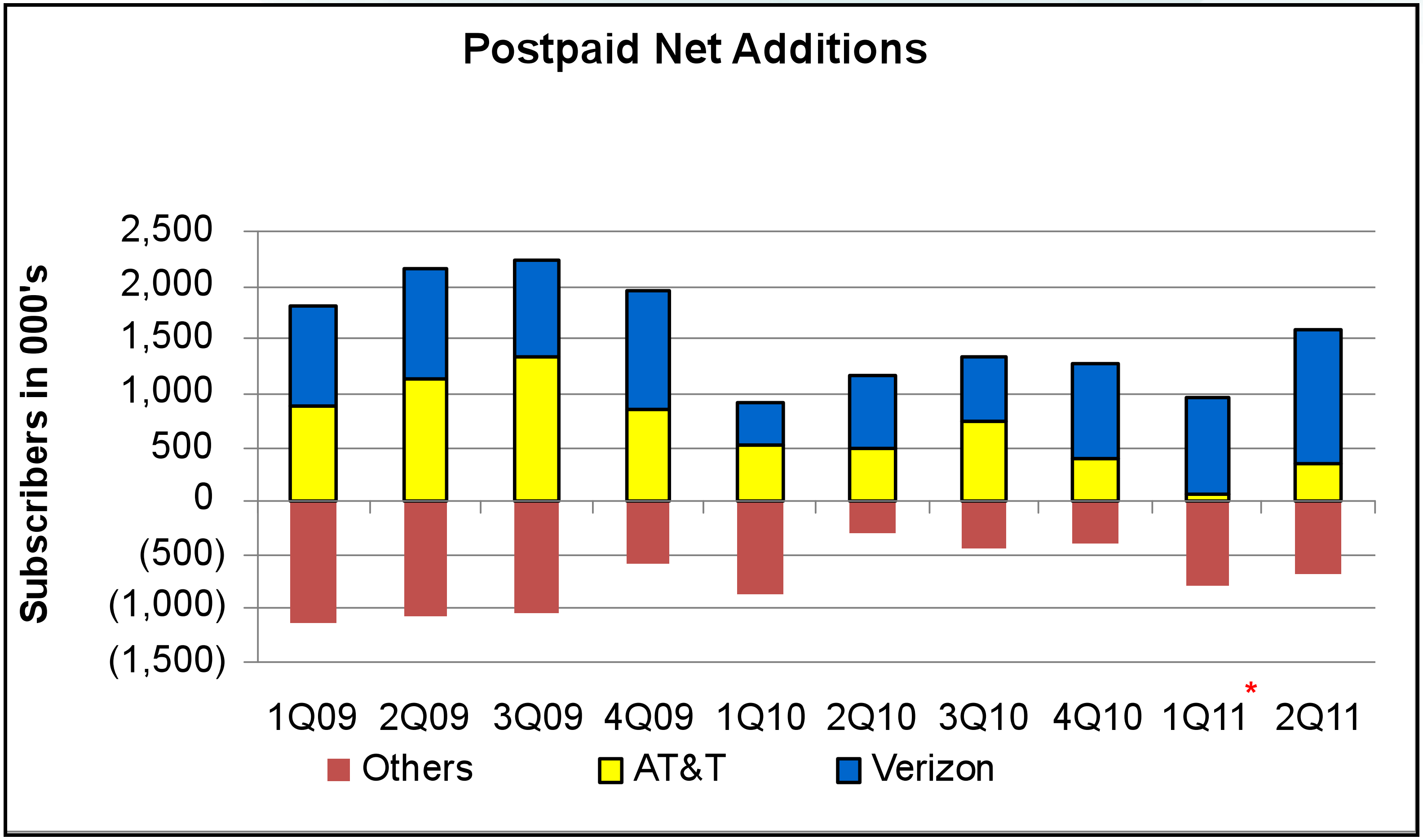
U.S. Cellular

# Constraints on Ability of Smaller Carriers to Compete

- Even within their own footprints, smaller carriers' survival is threatened by emerging market conditions
- Dominance of the larger carriers affects the ability of smaller carriers to compete both on a local/regional level, as well as a national level
  - Concentration has increased in all wireless markets
- Consumers demand access to a broad range of the latest and most advanced handsets.
- Consumers demand nationwide roaming capability, and increasingly, data and international roaming.
- Smaller carriers have difficulties obtaining sufficient spectrum.
- USCC is dependent upon AT&T and Verizon for special access.

U.S. Cellular

# AT&T and Verizon are Getting all of the Growth in Postpaid Subscribers




* Verizon launches iPhone

U.S. Cellular

# Strategic Conduct by Larger Carriers

- Exclusive contracts for the latest generation handsets
  - Handset availability drives market share
- AT&T was instrumental in post-auction definition of an LTE band tailored to the licenses won by AT&T - effectively restricting interoperability
- AT&T and Verizon engage in aggressive, strategic spectrum acquisition
  - Both have extensive unused spectrum
  - FCC auction rules have favored larger companies
- Supracompetitive special access prices
- AT&T and Verizon oppose regulatory action
  - Data roaming requirements
  - Restrictions on handset exclusivity
  - Special access reform
  - 700Mhz device interoperability

U.S. Cellular

# Merger Combines 2 of the 4 Large Nationwide Carriers

- Post-merger, only two companies will control approximately 80% of the wireless market

- Combines the only two significant GSM carriers

- Elimination of T-Mobile will have other negative repercussions:
  - Today, T-Mobile is a purchaser of special access and roaming services – an important customer for alternate providers of access where they do exist.
  - T-Mobile is a potential LTE roaming partner for smaller carriers
  - Often allied with smaller carriers in regulatory proceedings
    - Lessens number and strength of participants in the regulatory process that are not aligned with AT&T and Verizon

U.S. Cellular

# Effects of the Merger

**The merger threatens significant competitive harm**

- Today, even absent the merger, the smaller carriers like USCC are limited in their ability to constrain the larger carriers from exercising market power

- More extensive conditions are necessary to ensure that this merger does not increase market power and exacerbate the competitive disadvantages of the smaller carriers

- Remedies limited to those obtained in prior wireless mergers would be inadequate

- The merger presents an opportunity to obtain significant changes that would make smaller carriers more competitive

# Merger Could Exacerbate Handset Access Constraints

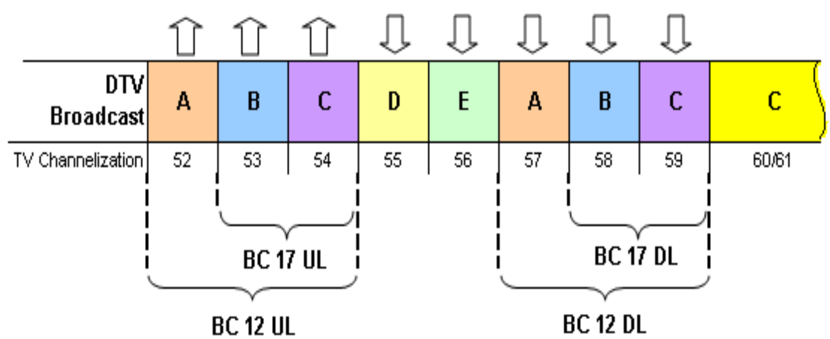
**Handset exclusivity has created a competitive disadvantage for smaller carriers and increased market concentration**

- Large carriers are more attractive to handset manufacturers seeking exclusive partners because of their scope and large number of customers
- Conversely, large carriers may also be able to extract exclusive deals from manufacturers by threatening not to carry a handset at all without an exclusive deal.
- The larger a carrier becomes, the more powerful that threat becomes, and the costs of exclusivity are correspondingly reduced to the manufacturer because of reduced opportunity costs
- Thus, the merger is likely to result in AT&T having a greater ability to obtain exclusive deals for handsets
- Merger approval should be conditioned on AT&T agreeing not to enter into exclusive handset deals
  - Such a condition would make handset manufacturers less likely to make an exclusive deal for any handset with any carrier

U.S. Cellular

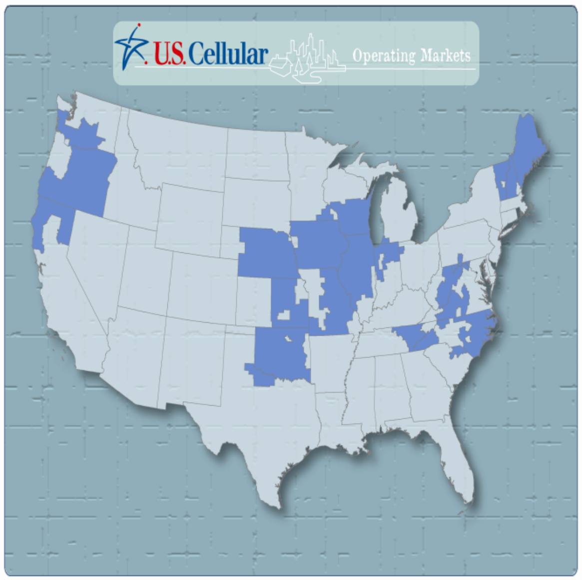
# FCC Should Ensure Handset Interoperability

- T-Mobile could exert pressure on handset manufacturers to produce interoperable phones
- Historical precedent for requiring interoperability
  - The Commission required interoperability between the original A & B cellular blocks
    - Policy intended to encourage competition through development of A block
    - Prevent the wireline incumbents (B block) from having too large of an advantage
- Require that AT&T include band class 12 in all AT&T devices that operate in 700Mhz

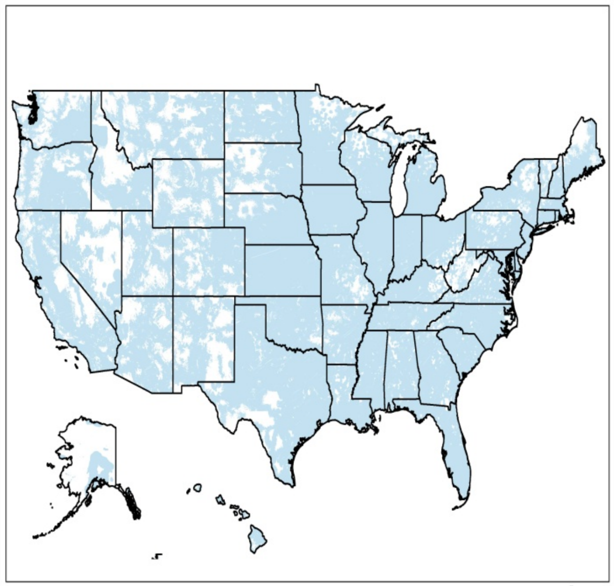


# Smaller Carriers Depend on Roaming to Compete

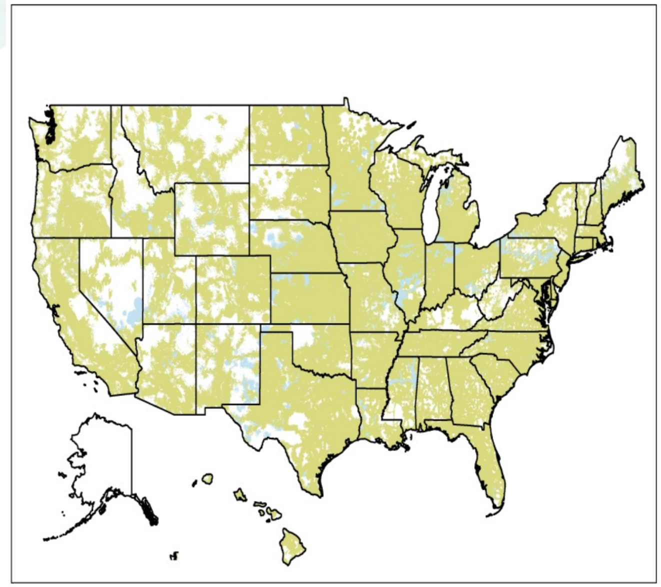
- Smaller Carriers such as USCC have relatively small in-market footprints, yet consumers demand nationwide voice/data packages




US Cellular operating footprint without roaming



US Cellular operating footprint with voice roaming



US Cellular operating footprint with date roaming

- Ability to obtain voice and data roaming, including LTE roaming, at competitive rates is essential

U.S. Cellular

# Smaller Carriers Depend on Roaming to Compete

- Merger reduces from 4 to 3 the number of potential nationwide LTE roaming partners
  - Together with the fragmentation of LTE band classes, this will impede the ability of smaller carriers to roam

- Merger hurts even CDMA carriers like USCC that are moving to LTE

- T-Mobile, absent the merger, could have been a reciprocal partner with USCC for LTE roaming and a large purchaser of roaming services from USCC and other rural wireless carriers.

U.S. Cellular

# Require AT&T to Offer Roaming on Competitive Terms

- Merger presents an opportunity for the Commission to strengthen its existing roaming orders to address increased market power
- Potential Mechanisms:
  - Require AT&T to comply with the data roaming order, regardless of litigation outcome
  - Require AT&T to agree to accelerated arbitration if carriers can not agree on rates and other terms in a commercially reasonable period
    - Arbitration schedule with accelerated time limits, including deadlines for staff and final Commission decisions
    - Independent review of claims of technological incompatibility
    - Given increased market power, the burden of proof should be on AT&T
- Roaming remedy will only be effective if it also addresses interoperability issues

U.S. Cellular

# Limitations on Spectrum Acquisitions

- The Commission should analyze the acquisition of capacity as a merger
  - Spectrum is equivalent to capacity
  - 2010 FTC and DOJ Horizontal Merger Guidelines note that in some industries, market share should be calculated by available capacity: "*In such markets, capacities or reserves may better reflect the future competitive significance of suppliers than revenues, and the Agencies may calculate market shares using those measures*."
  - Limitations should be imposed to prevent further excessive concentration of spectrum
- The Commission has imposed spectrum caps in the past, and the competitive market in wireless and PCS services developed while spectrum caps were in place
- In addition to imposing conduct-related conditions and operational divestitures, the Commission should require spectrum divestitures in excess of certain thresholds
- Spectrum divestitures should be structured to ensure that they strengthen multiple competitors in both urban and rural markets.
  - Spectrum sales should not be bundled on a national or super-regional basis
  - Limits on amount of spectrum acquired by any single carrier
  - Ensure existence of robust infrastructure and device ecosystem in divested bands

U.S. Cellular

# Special Access Terms and Conditions

- Small and regional carriers need increasing access to cell sites every year.
  - This need becomes more acute as they increasingly need to deploy metro (small) cells within the larger macro cells
  - The amount of bandwidth required for each cell is also increasing because of expanding data usage

- AT&T and Verizon, the two largest wireless carriers, are also huge wireline carriers with monopoly or near-monopoly backhaul facilities in many locations

- Supracompetitive pricing of backhaul benefits the two largest wireless carriers, which are also wireline carriers
  - AT&T has increased special access rates above what they would be in a competitive market

U.S. Cellular

# Special Access Remedy

- T-Mobile is a large unaffiliated carrier and purchaser of special access
  - Can leverage lower prices
  - Helps to establish benchmark competitive rates

- Possible solutions:
  - Require arbitration in special access negotiations
  - Benchmark rates to competitive areas
  - Non-discrimination requirements
  - Prohibit bundling of circuits/Require pricing on a standalone basis

U.S. Cellular

# Operational Divestitures

- Divestitures will be necessary to protect competition in regional markets

- Divestitures in prior wireless mergers have been problematic
  - Divestitures were not of stand-alone businesses
  - Transitions are complex and time-consuming
  - Opportunities for mischief abound
    - Insufficient duration of transition agreements; significant penalties
    - Failure to identify and divest appropriate employees
    - Significant poaching of customers by merging party during transition

- Added challenge in this case because divested network will be GSM
  - No substantial potential GSM acquirers remain

U.S. Cellular

# Divestitures Must Be Open to Smaller Carriers

- Any divestitures in this case should be meaningful and substantial
- Should include:
  - Substantial spectrum capacity
  - Large enough scale to justify operating a GSM network until LTE transition is complete
  - Adjacency to existing operations of USCC and other smaller carriers
  - Sufficient information made available to prospective purchasers to enable adequate due diligence
  - Longer transition period – acquirer option to obtain transition services for up to 3 years
  - Strong, enforceable prohibitions on the poaching of employees or customers
    - Restrictions on advertising in divested markets during transition period
    - Require AT&T to include provisions in divestiture contracts that protect purchaser
      - Compensation to acquiring carrier for customers recaptured by AT&T
    - Ensure that purchasers can use contract to enforce obligations under the decree
  - Access to seller's procurement agreements for handsets and equipment

U.S. Cellular

# Conclusion

- Small carriers face considerable challenges competing with the Big 4 even absent the merger and the merger will exacerbate these problems
- In order for smaller carriers to provide a competitive check on the market power of AT&T and Verizon, the merger must include robust conditions that go beyond divestitures of operations or spectrum
  - The merger presents a unique opportunity for the Commission to address the underlying competitive issues in wireless markets to achieve a more competitive outcome
- Remedies discussed herein are interrelated; they will not be effective on a stand alone basis
  - Ensure access to handsets; prohibit exclusivity
  - Mandate interoperability (lower 700Mhz and other bands)
  - Access to voice and data roaming, including LTE roaming and feature functionality, on competitive terms
  - Regional/local divestitures of operations (including substantial spectrum capacity)
  - Spectrum divestitures and limits on spectrum acquisitions
  - Ensure special access on competitive terms

U.S. Cellular